



CANADIAN RESERVE
OIL AND GAS LTD.

1976 ANNUAL REPORT



CANADIAN RESERVE OIL AND GAS LTD.

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ANNUAL MEETING

The Annual General Meeting of Shareholders of the Company will be held at the Calgary Convention Centre, Calgary, Alberta, on April 19th, 1977 at 10:00 a.m. (Calgary Time).

CORPORATE INFORMATION

DIRECTORS

John R. McMillan, Los Angeles
Chairman of the Board and Chief Executive Officer,
Reserve Oil and Gas Company

Howard C. Pyle, Los Angeles
Petroleum Investments

Newton T. Bass, Apple Valley
Chairman of the Board, Emeritus,
Reserve Oil and Gas Company

Paul D. Meadows, Denver
President and Chief Operating Officer,
Reserve Oil and Gas Company

Maclean E. Jones, Q.C., Calgary
Partner
Jones, Black & Company

***B. J. Westlund**, Lake Oswego, Oregon
Retired Businessman

Cortlandt S. Dietler, Denver
President, Western Crude Oil, Inc.

R. Bruce Bailey
President, Canadian Reserve Oil and Gas Ltd.

Harry Hole, Edmonton
Vice-President, Lockerbie and Hole Western Limited

OFFICERS

John R. McMillan
Chairman of the Board and Chief Executive Officer

Paul D. Meadows
Chairman of the Executive Committee

R. Bruce Bailey
President

J. Edouard Michaud
Vice-President

Joe R. Dundas
Vice-President

David W. Talbot
Vice-President and Secretary Treasurer

Grant D. Richards
Assistant Secretary and Assistant Treasurer

Tom L. Deen
Assistant Secretary

HEAD OFFICE

639 - 5th Avenue S.W.,
Calgary, Alberta

AUDITORS

Arthur Young, Clarkson, Gordon & Co.
Calgary, Alberta

REGISTRAR

GUARANTY TRUST COMPANY OF CANADA
Calgary, Alberta

TRANSFER AGENT

GUARANTY TRUST COMPANY OF CANADA
Calgary, Alberta; Vancouver, British Columbia;
Toronto, Ontario; Montreal, Quebec

STOCK EXCHANGE LISTINGS

TORONTO STOCK EXCHANGE
**MONTREAL STOCK EXCHANGE

*Retired from the Board of Directors effective October 15, 1976.

**Ceased trading on Montreal Stock Exchange November 22, 1976.

HIGHLIGHTS 1976

	1976	1975	% Change
Gross revenue	\$16,111,028	\$13,556,358	+19
Cash flow	\$ 9,401,042	\$ 7,146,727	+32
Per share	\$.98	\$.74	
Net income	\$ 5,197,614	\$ 4,319,334	+20
Per share	\$.54	\$.45	
Working capital at year end	\$ 3,919,366	\$ 3,280,956	+19
Property and equipment additions	\$ 9,177,555	\$ 5,275,725	+74
Oil and gas liquids sales (before royalty deduction)			
Barrels	1,819,981	2,190,688	-17
Barrels per day	4,973	6,002	
Gas sales (before royalty deduction)			
Mcfs	7,818,312	7,266,045	+ 8
Mcfs per day	21,362	19,907	
Wells drilled — net			
Oil	8	12	
Gas	10	2	
Dry	12	10	
Total	30	24	
Acreage — net working interest	1,724,140	3,626,714	-53
Outstanding shares	9,640,437	9,635,037	





to the SHAREHOLDERS

It gives me a great deal of pleasure to report a year of continued growth by Canadian Reserve. Virtually all segments of the Company's operations continued to expand as planned. The Company participated in the drilling of 99 wells in western Canada, up significantly from the 56 wells drilled in 1975.

As a result of higher prices for crude oil and natural gas, and increased production volumes of natural gas, the Company can report a record financial performance for the year ended December 31, 1976. Gross revenues increased by 19% to \$16,111,000 and cash flow increased by 32% to \$9,401,000 or \$.98 per share. Cash flow before income tax was \$10,412,000 or 17% greater than in 1975. Net income increased 20% to \$5,198,000 or \$.54 per share as compared with \$.45 per share for the previous year.

Gross sales of crude oil and natural gas liquids declined in 1976 to 4,973 barrels per day from the previous year of 6,002 barrels per day; however, gross natural gas sales increased from 19.9 MMcf per day to 21.4 MMcf per day. The reduction in gross sales of crude oil and natural gas liquids is a direct result of restrictions in the export of heavy crude oil to the United States. As a consequence, the Company shut in approximately 30% of its heavy crude oil productive capacity.

Gross sulphur sales for the year totalled 59,600 long tons at an average price of \$13.09 per long ton as compared to gross sales of 42,295 long tons at an average price of \$21.40 per ton in 1975. Sales volumes should be maintained in 1977; however, no improvement in the price per long ton is expected.

Changes in wellhead prices in Alberta and British Columbia have successfully stimulated exploration efforts. The situation in Saskatchewan, however, remains unchanged with industry, including Canadian Reserve, preferring to spend its exploration funds in areas where an acceptable return on investment can be expected.



The Company continued the efforts to establish natural gas projects in Alberta during 1976. These efforts, successful in finding significant new natural gas reserves, received a serious setback in late 1976 when major purchasers of natural gas in Alberta announced that they would not be entering into any new natural gas contracts during 1976 and 1977. As a consequence of this announcement, Canadian Reserve abandoned most of its plans for development of natural gas reserves in several areas in Alberta including: Atlee-Buffalo, Cessford, Bow Island, Beaverhill Lake, Rainbow South and Gull Lake.

In British Columbia, your Company, as predicted in the 1975 report to shareholders, achieved first sales of natural gas from new wells at Kotcho Lake. This production of some 4 MMcf per day, together with approximately 1 MMcf per day of natural gas sales from the Firewood-Jeans area, contributed significantly to the overall increase in natural gas sales for 1976.

In spite of the unfavorable economic rewards, Canadian Reserve, in 1977, has plans for a renewal of exploration and development in the heavy crude oil areas of the Province of Saskatchewan. This renewed interest arises from a major announcement by the National Energy Board in late 1976, removing heavy crude oil from light and conventional crude oil restrictions and placing the export of heavy crude oil under a separate licencing system. This system should allow all heavy crude oil production, in excess of Canadian needs, to be marketed in the United States. The Company is optimistic that the National Energy Board, in its recommendations to the federal government, will take steps to provide for permanent solutions to the problems associated with the marketing of heavy crude oil. In addition, Canadian Reserve believes that improved net back value will accrue to producers of heavy crude oil in the near future.

Your Company is participating in enhanced recovery schemes encompassing in-situ combustion and steam injection in the Bodo field of east central Alberta, and is investigating additional recovery techniques. Both the federal and provincial governments have made funds available for pilot projects in the heavy crude oil areas. Canadian Reserve, together with other industry participants, plans to make use of the funds which are allocated for further study of enhanced recovery techniques in 1977.

Canadian Reserve has planned an active exploration and development program for the forthcoming year. The Company plans to participate in or drill approximately 160 exploratory and development wells in western Canada during 1977. As in previous years, the major portion of cash flow will be utilized in exploration and development in western Canada.

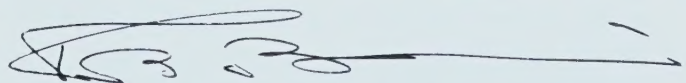
The fiscal year 1976 was a very satisfying year for Canadian Reserve Oil and Gas Ltd. A summation of the year indicates that the goals of the Company are being achieved. While we are proud of the Company's record, we know that what has been accomplished is not nearly so important as what your Company does in the future, and the development of a sound

relationship between business and government is vital to continued progress. Too often in the past, government and industry have assumed adversary positions. The failure of this approach is apparent in the deterioration in Canada's energy position. The Company is confident that our governments now realize the very important role the private sector must be permitted to play if Canada is ever again to achieve self-sufficiency in crude oil. Large investments are required to find sources of crude oil and natural gas. If governments provide the proper economic environment, your Company will continue to conduct an aggressive exploration program in the very vital search for new reserves of crude oil and natural gas.

In the course of the year, B. J. Westlund resigned from the Board of Directors. We express thanks to Mr. Westlund for his contribution to the Board of Directors. Further, we welcome to the Board of Directors, Harry Hole, Vice-President and General Manager of Lockerbie and Hole Western Limited. Mr. Hole is a native Albertan, residing in the City of Edmonton.

The achievements of the past year are due, in large part, to the efforts of the employees of the Company. The Board of Directors appreciates this dedication, and it is a pleasure for me to express thanks to the employees for their continued outstanding performance and support.

For the Board of Directors,

A handwritten signature in dark ink, appearing to read 'R. B. Bailey', with a long horizontal flourish extending to the right.

R. B. Bailey,
President.

EXPLORATION, DEVELOPMENT and OPERATIONS

Canadian Reserve, as a consequence of unstable markets, continued in 1976 to reduce the emphasis on heavy crude oil projects. Accordingly, the Company expended virtually all of its cash flow on new exploration projects and development drilling in prospective natural gas areas in Alberta and British Columbia. This effort was successful in increasing the Company's natural gas reserves by 8.8 Bcf during 1976 after production of 7.8 Bcf for the same period of time. Of the 99 wells drilled in western Canada in which the Company participated in 1976, 65 were drilled primarily in search of natural gas. A summary of the Company's significant activities in 1976 follows:

EXPLORATION and DEVELOPMENT

BRITISH COLUMBIA

Higher prices for natural gas in the Province of British Columbia during 1976 generated an increase in drilling activity. Canadian Reserve participated in the drilling of 12 (3.9 net) wells in British Columbia.

Kotcho Area

In the Kotcho area, Canadian Reserve, with partners, participated in the drilling of 4 Slave Point wells and 1 Bluesky well; this drilling program resulted in 2 producing natural gas wells, the d-7-J well which open flow tested at 69 MMcf/d in the Slave Point Dolomite and drill stem tested 2.8 MMcf/d in the Bluesky Sand, and the a-5-J well which drill stem tested at 8 MMcf/d in the Slave Point Dolomite and 1.3 MMcf/d in the Bluesky Sand. A third well, a-42-J, tested natural gas in both the Slave Point Dolomite and the Bluesky Sand, but, on further evaluation, appears non-commercial. The b-A68-H well was placed on production from the Bluesky Sand.

The Company's plans include conducting a further 25 miles of reflection seismic and drilling 3 additional wells to test the Slave Point Dolomite in 1977.

Canadian Reserve has Working Interests which vary from 18.75% to 100% in 58,121 gross acres (27,592 net).



Suhm Area

Seismic operations conducted within this 9,100 acre Drilling Reservation have resulted in the Company selecting two Slave Point drilling locations. This prospect is located along a very favorable natural gas trend in northeastern British Columbia, and, in addition to the Drilling Reservation, in which Canadian Reserve holds a 37.5% Working Interest, the Company has under farmout or option agreement an interest in a





MMcf/d from approximately 60' of net pay. The Company has a 25% carried interest in the spacing unit for this well.

Tenaka Area

During 1976, Canadian Reserve, as operator, conducted 20 miles of seismic within a 15,000 acre farmin block in this area. The initial exploratory earning well is at present being drilled and should this effort be successful a followup well will be drilled in 1977. The Working Interest of Canadian Reserve in this block is 13.75%. The exploratory program is designed to prove up additional natural gas reserves in the reef trend where 2 previous successful wells, a-36-G and b-84-G, were drilled in 1972 and 1974.

Conroy-Dahl Area

These areas are underlain by potential Bluesky natural gas-bearing sands; the Company has a Working Interest in approximately 100,000 acres contained in two large blocks within the potential natural gas-bearing area.

At Conroy, Canadian Reserve holds a 33 $\frac{1}{3}$ % Working Interest in 36,000 acres and plans to drill at least one well in 1977. The Company plans to participate to the extent of a 25% Working Interest in 5 wells at Dahl; these wells will test the Bluesky Sands underlying a 64,000 acre farmin block.

further 8,600 acres in this general area. Canadian Reserve plans to participate in a further 10 miles of reflection seismic and at least two wells during 1977.

Helmet Area

This area attracted a great deal of industry interest in 1976. Canadian Reserve participated in 2 wells of which 1 (Pacific Helmet d-73-L) resulted in a natural gas producer; this well tested 3.5

ALBERTA

During 1976, Canadian Reserve participated in the drilling of 73 (18.3 net) wells in Alberta, resulting in 40 (7.8 net) natural gas producers and 15 (4.6 net) crude oil producers.

NATURAL GAS PROJECTS

As a consequence of an increase in natural gas prices, the Company directed its exploratory and development efforts toward finding and



developing natural gas reserves during 1976. The following is a summary of the main areas in which these efforts were carried out.

Atlee-Bufferlo

The Company, as a holder of a 50% Working Interest in a 14,720 acre block, participated in the drilling of 5 shallow Cretaceous Sands exploratory wells, of which all resulted in potential dual zone natural gas wells from the Milk River and Medicine Hat Sands.

Cessford Area

Canadian Reserve purchased jointly with a partner a 4,480 acre block within a shallow Cretaceous Sands prospect in this area. While no drilling has yet been conducted on this block by Canadian Reserve, industry has completed approximately 30 natural gas wells in this general area.

Gull Lake

The Company has completed a Cretaceous-Ostracod natural gas well within a 7,680 acre block in this area; this well open flow tested at 19.9 MMcf/d.

Rainbow South Area

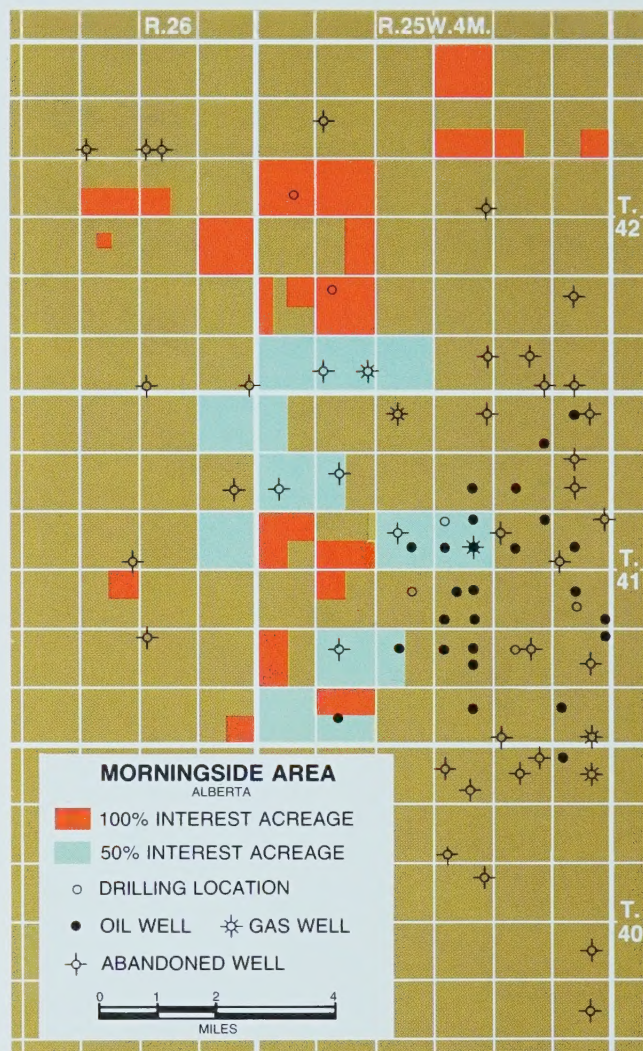
During 1976, the Company participated in the drilling of 2 Bluesky natural gas wells on two separate blocks, totalling 17,920 acres, in this northwestern Alberta area. Both wells were cased as potential natural gas producers. The Company plans to drill 2 additional wells in this area in early 1977.

Beaverhill Lake Area

The Working Interest of the Company in this area varies from 13.6% to 100% in approximately 11,840 acres. One joint well was drilled and cased in 1976 within this Cretaceous-Viking natural gas prospect. Approximately 10 natural gas wells in the area adjacent to this acreage have been drilled by industry.

Provost North Area

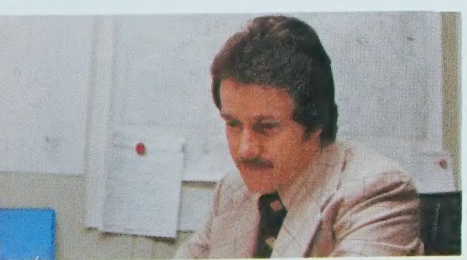
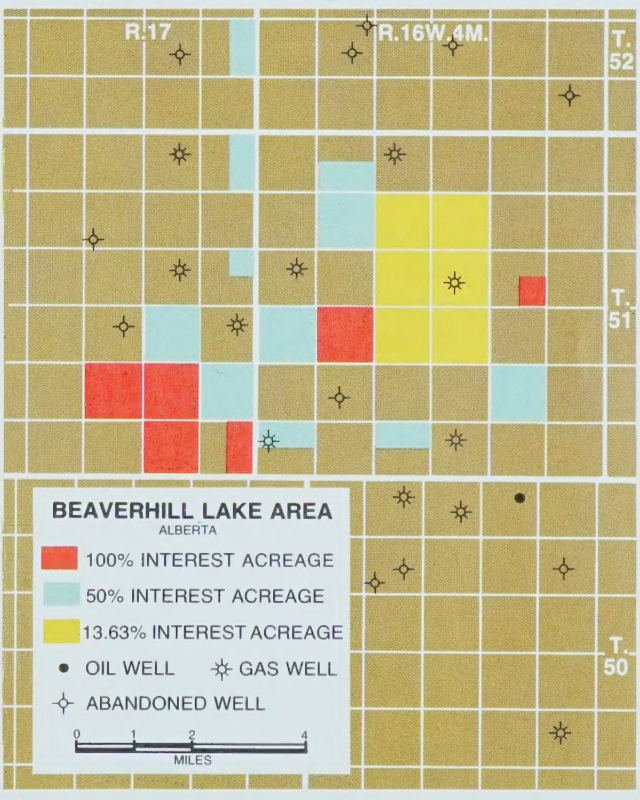
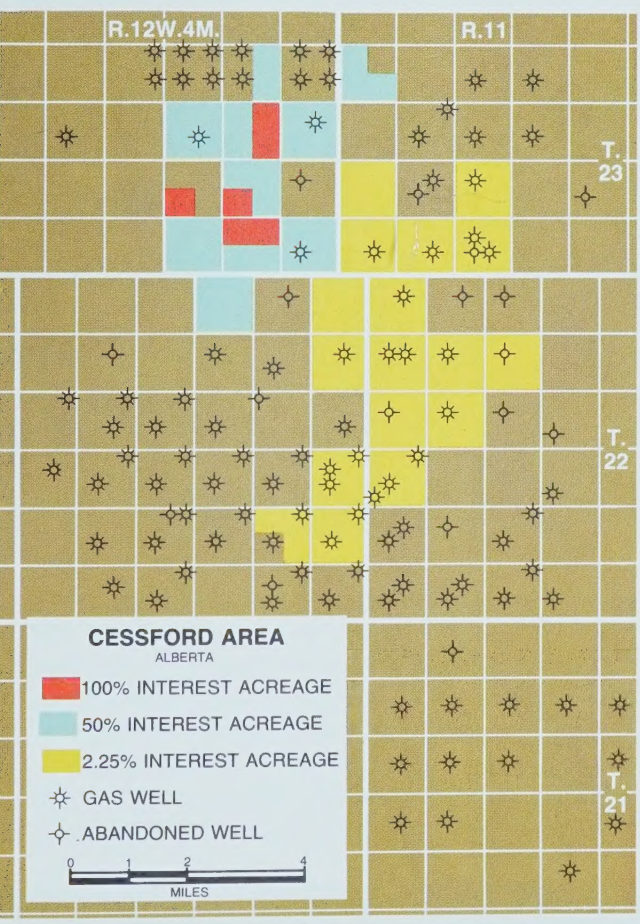
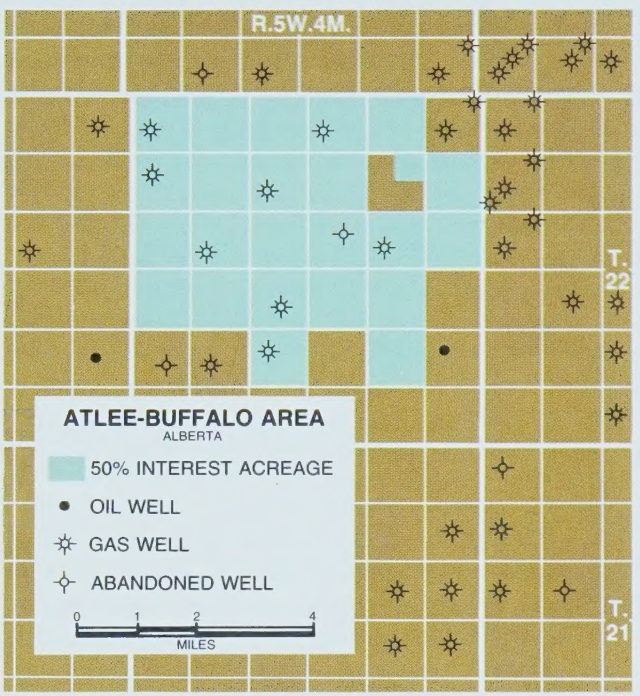
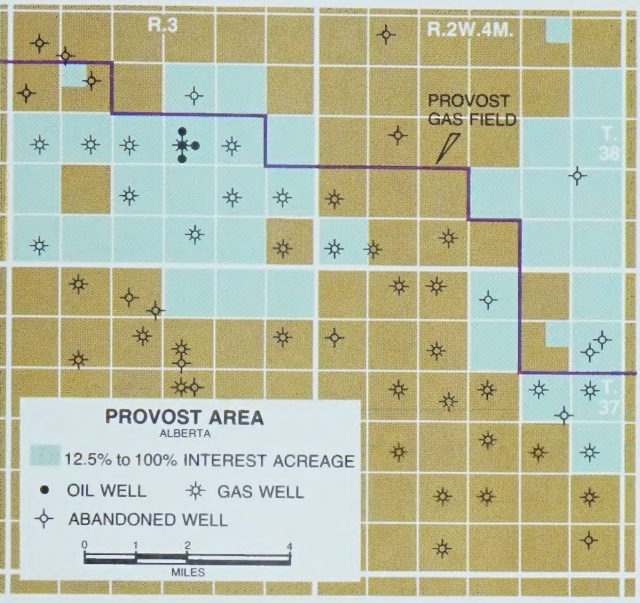
In early 1976, Canadian Reserve participated in the drilling of 13 wells (2.6 net) in this area of approximately 12,160 gross acres. This program resulted in 8 Viking natural gas wells, 2 Dina zone crude oil wells, and 1 Rex zone crude oil well. Further, a number of these wells are capable of natural gas or crude oil production from other zones.



MORNINGSIDE AREA

Three wells were drilled on these lands by a farmee at no cost to the Company. This program, together with 3 wells in which the Company joined as a 50% Working Interest partner, resulted in 4 Viking crude oil wells; 3 of the wells also have crude oil potential in the Glauconite Sand and 1 of such wells has natural gas potential in the Basal Quartz Sand. At present the farmee is drilling 2 additional wells in this area. The Company plans to drill several wells on this trend in 1977 mainly on those portions of the 12,000 acre block held 100% by Canadian Reserve.





HEAVY CRUDE AREAS — ALBERTA AND SASKATCHEWAN

During 1976, Canadian Reserve participated in 35 wells (12.6 net) in the heavy crude areas of Alberta and Saskatchewan, resulting in 15 crude oil wells (4.7 net), 9 natural gas wells (2.3 net), and 11 dry holes (5.6 net). Most of this drilling took place in the Bodo field as part of an ongoing development project and in the Senlac-Eyehill area of Saskatchewan where drilling was required to hold certain lands. As in 1975, extensive exploratory and development activities in these areas were curtailed because of unstable markets and inadequate economic returns.

FRONTIER AREAS

As a consequence of the Federal Government's land holding and royalty regulations, together with the high cost and risk of exploring in these areas, Canadian Reserve did not participate in any drilling during 1976. The Company has Working Interests, Royalty Interests and Carried Interests in over 7 million acres in the Arctic Islands and Northwest Territories. It does not plan any drilling in these areas in 1977.

HEAVY MINERALS EXPLORATION AND DEVELOPMENT

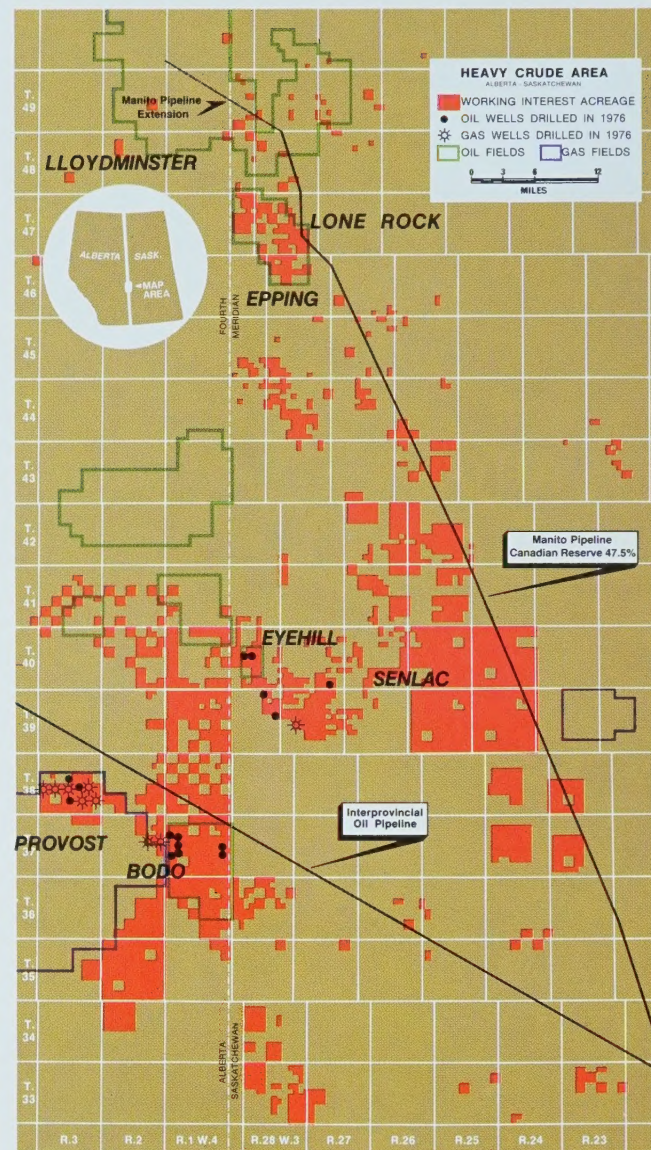
Exploration and development of heavy minerals were continued through 1976 as a joint venture program in the Rambler Hill area near Mayo, Yukon Territory. Percussion drilling totalling 7,700 feet was completed in this area. The Company does not plan further exploration and development until results of the drilling program have been analysed.

Operations at the Ironbridge properties in northern Ontario continue to be suspended pending a price increase for copper on the world market.

The Company's barite, lead, silver and zinc operation at the Homestake Mine at Kamloops, British Columbia remains suspended. The economics of resuming operations are at present being studied by Canadian Reserve as a consequence of the Provincial Government passing new mining legislation.

LAND

Canadian Reserve held Working Interests as of December 31, 1976, in 4.8 million acres (1.7 net) and overriding Royalty Interests in 5.5 million acres in the Western Canadian Sedimentary



Basin, Ontario, the Arctic Islands, eastcoast offshore, and the Yukon and Northwest Territories. This is a decline from December 31, 1975 due mainly to substantial surrenders being made in the Arctic Islands where the Company chose either to surrender or to assign its Working Interest in certain areas to avoid encountering high exploration commitments.





New purchases in the Western Canada Sedimentary Basin were limited to prospective areas where the Company will proceed with active exploration programs. These purchases were in the Swan Hills, Horburg, Groat Creek, Gull Lake, Cessford, Lloydminster, Panny River, Nanton, Morningside and Sampson areas of Alberta and the Conroy and Kotcho areas of British Columbia. Additional acreage was acquired through farmins also in Alberta and British Columbia as a result of the drilling of exploratory wells.

The Company granted numerous farmouts in 1976 resulting in substantial exploration activity on its acreage. The new Alberta Government Land Tenure Regulations, which became effective July 1, 1976, have been favorably received by the Industry. These changes should be advantageous to the Company as it will be in a position to capitalize on a faster turnover of land by the Industry, freeing a larger number of high quality prospects for potential acquisition.

SUMMARY OF ACREAGE HOLDINGS

Area	Working Interest		Royalty Interest	
	Gross	Net	Gross	Net
Yukon	209,626	129,576	48,632	1,459
Northwest Territories	691,760	359,546	664,165	19,055
Arctic Islands	1,645,909	502,269	4,405,870	76,300
Canadian Eastcoast Offshore	465,682	130,180	—	—
British Columbia	468,111	125,983	54,677	1,367
Alberta	812,081	284,058	131,842	3,296
Saskatchewan	509,739	189,282	187,807	1,041
Manitoba	7,472	1,870	1,396	35
Ontario	2,751	1,376	—	—
Total	4,813,131	1,724,140	5,494,389	102,553





COMPANY PROFILE

Canadian Reserve is an exploration, development and production Company involved in the natural resource industry, concentrating its efforts in the search for and development of natural gas and crude oil reserves in Canada. The Company has varying interests in petroleum and natural gas lands, pipelines, gas processing facilities, and mining properties.

Canadian Reserve is a successor to Fargo Oils Ltd. which was incorporated on November 20, 1950. Other companies were merged into Fargo Oils in 1958. Reserve Oil and Gas Company, in September 1967 purchased the 27% interest in the Company held by General American Oil Company and obtained the balance of the outstanding shares in 1968 through a share exchange. On April 18, 1969 the name was changed to Canadian Reserve Oil and Gas Ltd. On February 24, 1970 three other wholly owned Canadian subsidiaries of Reserve were amalgamated with Canadian Reserve. On February 8, 1971, 1,000,000 shares of Canadian Reserve were issued to the Canadian public.

Canadian Reserve has various interests in 10,307,520 acres of land located in Canada. This includes northern Canada and the east coast offshore. Notwithstanding these extensive land holdings, the Company concentrates its exploration and development efforts in the plains and foothill regions of western Canada. The major portion of the cash flow of the Company is invested in the search for crude oil and natural gas reserves in this area. The accompanying map shows the active prospect and producing areas of the Company.

Canadian Reserve Oil and Gas Ltd. is an Alberta Company headquartered in Calgary, Alberta with a district office at Lloydminster, Alberta. The Company employs 85 people, the majority being located in the Calgary office.





OPERATIONS

DRILLING

Exploratory completions totalled 52 wells, resulting in 9 oil wells, 16 natural gas wells and 27 dry holes for a success ratio of 48.0%. The interest of the Company in the successful exploratory completions resulted in 4.0 net crude oil wells and 5.8 net natural gas wells.

Canadian Reserve participated in the drilling of 47 development wells during 1976, equivalent to 9.0 net wells. Of these, 12 were completed as successful crude oil wells, 32 as successful natural gas wells and 3 wells were abandoned for a success ratio of 93.6%. The following chart illustrates in more detail the gross and net wells drilled in 1976.

Wells Drilled

	Gross Wells		Net Wells	
	1976	1975	1976	1975
Development				
Oil	12	14	3.3	6.8
Gas	32	5	4.4	1.3
Dry	3	2	1.3	1.1
	47	21	9.0	9.2
Exploration				
Oil	9	9	4.0	5.5
Gas	16	2	5.8	0.6
Dry	27	24	10.8	9.0
	52	35	20.6	15.1
Total Wells	99	56	29.6	24.3
			1976	1975
Average Well Participation ..			29.9%	43.4%
Success Ratio (Gross)				
Development			93.6%	90.5%
Exploration			48.0%	31.4%

PRODUCTION AND SALES

During 1976, the Company experienced a reduction in gross working interest crude oil and natural gas liquid sales. This reduction from a daily average during 1975 of 6,002 barrels to 4,973 in 1976 was a direct result of restrictions in the export of heavy crude oil to the United States; as a consequence, the Company shut in approximately 30% of its heavy crude oil productive capacity.

In October of 1976, the National Energy Board conducted Supply/Demand Hearings. Canadian Reserve, together with other industry representatives, appeared at these hearings for the purpose of highlighting the production and

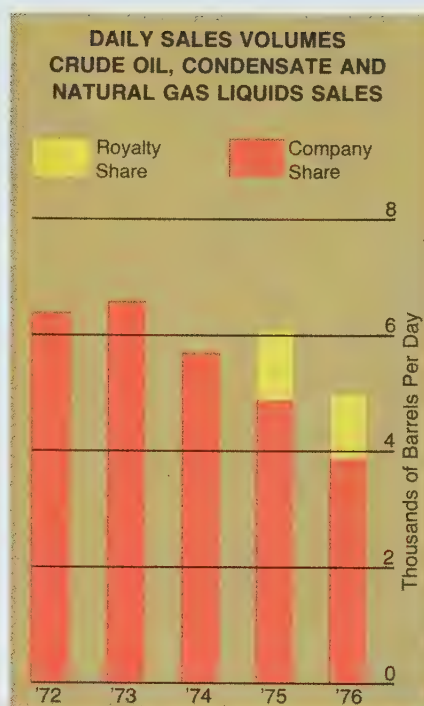
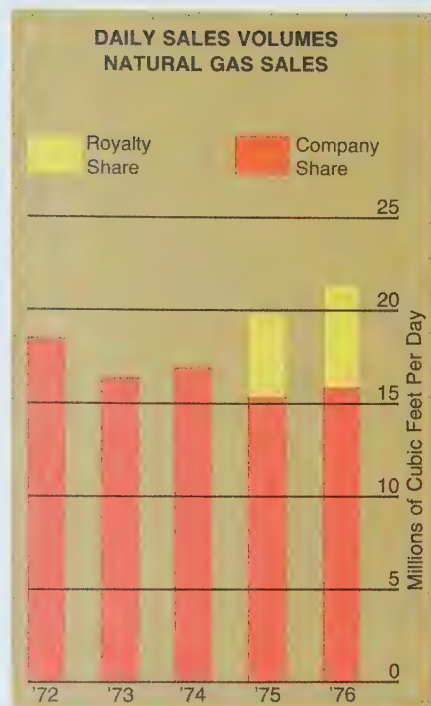
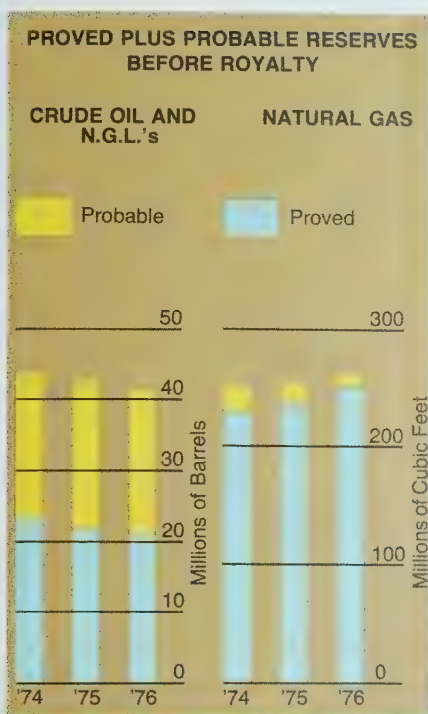
marketing problems associated with heavy crude oil; the Board was requested to allow all heavy crude oil volumes excess to Canadian domestic requirements to enter markets in the United States for a minimum period of 5 years. It is felt that this action would provide sufficient lead time to develop additional markets and increase heavy crude oil refining capacity in Canada. Further, it would stimulate exploration and development of additional heavy crude oil reserves. As a result of these hearings, the National Energy Board is expected to announce changes in heavy crude oil marketing sometime in early March of 1977.

In the interim, however, to alleviate the immediate problem of exporting heavy crude oil, the Board removed heavy crude oil from light and conventional crude oil restrictions and placed the export of heavy crude oil under a separate licencing system. This system should allow all heavy crude oil production, in excess of Canadian demands, to be marketed in the United States. The Company is optimistic that the National Energy Board, in its recommendations to the Federal Government, will take steps to provide for permanent solutions to the problems associated with the marketing of heavy crude oil. As a consequence of these positive measures by the Federal Government, Canadian Reserve is at present returning to full productive capacity and plans additional development drilling during the first half of 1977, contingent upon formalization of marketing arrangements.

NATURAL GAS PROCESSING

The Company owns interests in several natural gas processing plants in Alberta and operates a compression and dehydration system in the East Kotcho field of northeastern British Columbia.

In Alberta, Canadian Reserve owns a 33¹/₃% interest in the Lone Pine Creek processing facilities; these facilities treat sour and wet natural gas from the Lone Pipe Creek field. The Company's share of plant output during 1976 amounted to 1,849 MMcf of sales gas, 39,500 barrels of condensate and 12,969 long tons of sulphur. Further, Canadian Reserve owns an approximate 12% interest in natural gas processing facilities in the East Crossfield area, 30 miles northeast of Calgary. The Company's net share of sales of plant products from these facilities during 1976 amounted to 1,699 MMcf of sales gas, 15,600 barrels of condensate and 38,154 long tons of sulphur. From the facilities in the East Kotcho field of northeastern British



Columbia, a total of 3,396 MMcf of sales gas was processed during 1976. The Company's share of sales gas from these facilities amounted to 1,066 MMcf.

The daily average gross volumes of natural gas produced and sold by the Company in 1976 showed a substantial increase to a level of 21.4 MMcf/d, a gain of 8% over the 1975 daily average rate of 19.9 MMcf/d. However, sales of natural gas net to the Company's interest, after deduction of royalties averaged 16.0 MMcf/d in 1976, which approximates the 1975 average of 15.3 MMcf/d. Gross sales volumes were up substantially but net volumes were not because of the Province of Alberta's increasing royalty rate and a reduced demand for natural gas.

An increase of approximately 13% in natural gas sales net to the Company's interest can be expected in 1977 because of new reserves which will come on production. This increase, combined with anticipated higher gas prices, should result in substantially greater gas sales revenues to the Company.

Gross working interest sulphur production during 1976 amounted to 140 long tons per day, a decrease of 8% from the 152 long tons per day in 1975. The Company sold 59,600 gross long tons during 1976 for an average net back price of \$13.09 per long ton, which compares to the average net back price of \$21.40 per long ton received in the previous year. The increased

sales exceeded production over that experienced in 1975 resulting in a reduction of the Company's field inventory of sulphur.

TRANSPORTATION

Canadian Reserve owns a 47.5% interest in the 101 mile Lone Rock-Kerrobert pipeline system which transports a crude oil-condensate blend from the Lloydminster area of Saskatchewan to Interprovincial Pipeline at Kerrobert, for ultimate delivery to the Ontario and Chicago marketing areas. During 1976 this pipeline delivered 2,203,948 barrels of blend to the Interprovincial Pipeline, an average of 6,038 barrels per day; this was a decrease of 1,882 barrels per day from the 1975 average of 7,920 barrels per day. This reduction was a result mainly of a decrease in heavy crude oil markets and less exploratory and development drilling. The Lone Rock-Kerrobert pipeline system will be extended approximately 14 miles from Lone Rock, Saskatchewan to the Blackfoot area of Alberta. The complete system will now be under the jurisdiction of the National Energy Board and will operate as Manito Pipelines Ltd. The Company expects that this extension will be completed during February of 1977.

RESERVES

The remaining recoverable hydrocarbon reserves of Canadian Reserve at December 31, 1976, as estimated by the Company's engineering staff,

are illustrated in the included table. Further, a comparison of the proved and probable reserves for the years 1974 through 1976 are illustrated in the graph. The Company's natural gas reserves increased by 8.8 Bcf during 1976 after production of 7.8 Bcf during the year. Crude oil and natural gas liquids reserves, however, decreased by 1,096,000 barrels after production of 1,820,000 barrels. The estimated proved and additional probable reserves include only those which can be classified as proved and probable in accordance with accepted American Petroleum Institute standards. The crude oil reserves do not

include significant volumes of potential heavy crude oil which are capable of recovery through thermal recovery techniques. All reserves have been calculated before royalty deductions.

RESERVES

Before Deducting Royalty

	Crude Oil (Barrels)	Natural Gas Liquids (Barrels)	Natural Gas (Millions of Cubic Feet)
At December 31, 1976			
Proved	18,818,000	1,745,000	251,811
Probable	21,147,000	63,000	12,125
TOTAL	39,965,000	1,808,000	263,936

CRUDE OIL, CONDENSATE AND NATURAL RESOURCES

	CRUDE OIL AND CONDENSATE SALES				NATURAL GAS SALES			
	1976		1975		1976		1975	
	Gross WI	Net WI	Gross WI	Net WI	Gross WI	Net WI	Gross WI	Net WI
BRITISH COLUMBIA								
Blueberry	59,700	31,400	84,900	41,300	251,100	245,900	283,300	285,300
Inga	65,400	34,400	59,900	31,000	288,700	284,700	248,200	248,800
Kotcho	—	—	—	—	1,065,700	1,065,700	210,700	203,900
Jeans-Fireweed	—	—	—	—	356,100	354,100	—	—
Other fields	500	1,000	1,800	1,800	14,800	16,100	111,100	105,700
	125,600	66,800	146,600	74,100	1,976,400	1,966,500	853,300	843,700
Distribution (%).....	6.9		6.7		25.3		11.7	
ALBERTA								
Bodo	61,800	46,700	32,400	25,300	1,200	1,100	4,300	3,800
Cessford	—	—	—	—	162,000	96,400	189,600	123,900
Crossfield	40,300	30,000	50,800	42,400	844,900	594,500	854,800	617,900
Crossfield East	31,600	21,000	30,800	20,800	1,698,700	1,124,000	1,741,100	1,183,200
Fenn Big Valley	24,600	15,600	52,000	33,400	800	700	1,200	900
Lobstick	2,100	1,800	1,900	1,600	—	—	—	—
Lone Pine Creek ...	39,500	26,900	52,400	39,400	1,848,600	1,181,500	2,412,300	1,830,300
Medicine Hat	—	—	—	—	74,700	65,500	40,600	33,900
Medicine River	130,500	91,100	113,800	82,100	953,800	598,500	893,500	706,900
Pembina	146,200	98,000	162,100	111,400	44,500	36,600	49,300	42,800
Swan Hills	50,600	28,600	57,000	34,000	30,000	19,000	33,500	23,500
Other fields	59,900	51,600	48,900	33,500	152,000	130,400	152,900	141,600
	587,100	411,300	602,100	423,900	5,811,200	3,848,200	6,373,100	4,708,700
Distribution (%)	32.3		27.5		74.3		87.7	
SASKATCHEWAN								
Battle Creek	5,300	4,600	8,200	7,300	—	—	—	—
Cantuar	11,000	10,100	24,900	21,100	—	—	—	—
Flat Lake	32,000	25,400	34,200	28,300	—	—	—	—
Forget	36,600	26,700	42,900	34,000	—	—	—	—
Lone Rock/Epping ..	870,600	742,100	1,154,200	1,055,400	—	—	—	—
Steelman	42,500	33,000	47,300	37,800	—	—	—	—
Other fields	39,600	34,100	53,500	26,400	30,700	26,500	39,700	36,900
	1,037,600	876,000	1,365,200	1,210,300	30,700	26,500	39,700	36,900
Distribution (%)	57.0		62.3		0.4		0.6	
MANITOBA								
North Virden	59,300	49,400	67,700	55,100	—	—	—	—
Other fields	10,400	10,400	9,100	9,000	—	—	—	—
	69,700	59,800	76,800	64,100	—	—	—	—
Distribution (%)	3.8		3.5					
	1,820,000	1,413,900	2,190,700	1,772,400	7,818,300	5,841,200	7,266,100	5,589,300



FINANCIAL REVIEW

GROSS REVENUE

Gross revenue increased \$2,555,000 to \$16,111,000 for the year 1976. The increase is the result of improvement in prices of crude oil, natural gas, natural gas liquids, and an increase in sales of natural gas.

Sales statistics in previous annual reports have been shown after the deduction of royalty interest volumes. However, increasing provincial royalties has made the comparison from year to year misleading with regard to annual changes in producing rates. Therefore, sales volumes included in this report, unless otherwise specified, are presented before the deduction of royalties.

Crude oil sales for the year averaged 4,973 barrels per day, a decrease of 17% from 1975. The marketing problems associated with heavy crude oil accounted for 82% of this decrease. Crude oil sales provided approximately 51% of the Company's gross revenue.

Crude oil prices continued to improve with a 17% increase in the per barrel average from \$6.56 in 1975 to \$7.71 in 1976. Natural gas liquids prices rose from an average of \$6.91 per barrel for 1975 to \$7.51 per barrel for 1976.

Natural gas sales increased 8% in 1976 with increased production from the Kotcho area in British Columbia more than offsetting production declines in Alberta. The 1976 sales averaged 21.4 MMcf per day at an average price for the year of \$.89 per Mcf, a 60% increase over the 1975 average. Natural gas sales provided 30% of gross revenue as compared to 21% in 1975.

Sulphur prices declined during the year from an average for 1975 of \$21.40 per long ton to \$13.09 per long ton for 1976. A substantial increase in the volume of sulphur sales offset most of the revenue lost due to the price drop.

CASH FLOW

Cash flow generated from operations, which consists of net income before deduction of all non-cash items, increased \$2,254,000 or 32% to \$9,401,000 for the year. These funds, equivalent to \$.98 per share, financed all of the Company's capital expenditures incurred during the year. Cash flow before income taxes was \$10,412,000 or \$1.08 per share, 17% above the comparative total for 1975.

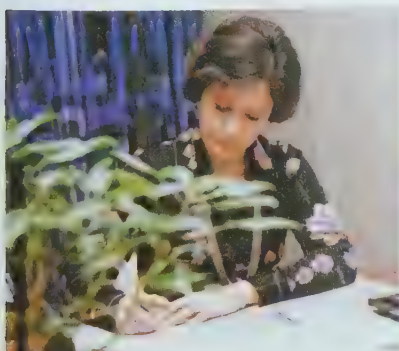
DEPRECIATION AND DEPLETION

Depreciation and depletion expenses increased \$541,000 or 25% to \$2,707,000. The write-offs for oil and gas properties and production equipment are based on the unit-of-production method. This method takes into account the Company's share of the total net volume of oil and natural gas and product sales for the year in relation to the total net reserves expressed in equivalent barrels of crude oil. Natural gas and sulphur are converted to equivalent barrels of crude oil based on the year end unit values of each. As the price of natural gas had a much greater rate of increase than the price of crude oil during 1976, the equivalent barrels of reserves of natural gas were increased substantially over those computed at the end of 1975. This calculated increase in reserves, together with the decrease in sales volumes, partially offset the increase in write-offs due to the substantial capital expenditures made in 1976.

INCOME TAXES

Provision for income taxes were in total about the same as in 1975. However due to the increased write-offs available for tax purposes as the result of higher capital expenditures in 1976, a greater proportion of the tax has been deferred to future years.

Under the 1974 revision of the Federal tax laws, all income receivable by governments from the Company properties, through royalties, royalty surcharges or similar payments, are deemed





income to the Company for tax computation purposes. Such non-deductible payments to governments by the Company during 1976 amounted to approximately \$7,111,000 and the cumulative to date since May, 1974 is \$18,631,000.

NET INCOME

Net income increased \$878,000 to \$5,198,000 for 1976. This resulted in \$.54 per share in 1976 as compared to \$.45 per share in 1975.

PROPERTY AND EQUIPMENT ADDITIONS

Property and equipment additions in 1976 amounted to \$9,178,000 up 74% from 1975. The distribution of 1976 expenditures was \$4,288,000 for the drilling of wells, \$1,360,000 for leasehold acquisitions, \$1,233,000 for well and lease equipment, \$432,000 for other facilities, \$752,000 for exploration overhead, \$299,000 for delay rentals, and \$814,000 for geological, geophysical and other. The geographical distribution of these expenditures was: Alberta 54%; British Columbia 31%; Saskatchewan 8%; Foreign 6%; and other areas 1%.

WORKING CAPITAL

Working capital at year end totalled \$3,919,000 compared to \$3,281,000 a year earlier. The working capital ratio increased from 1.7:1 to 2:1.

PRODUCTION LOANS

Production loans at December 31, 1976 were \$1,490,000 of which \$600,000 is payable during 1977 and thus has been included in the current liabilities. The Company obtained \$400,000 of new loans during 1976.

1977 OUTLOOK

The Company's outlook for 1976 was based on the continuation of an improved attitude of government toward the resource industry and our estimates for major income categories of increases of 20% to 25% and a capital expenditures increase of 50% turned out to be reasonably accurate. For 1977, our assessment of government attitudes in general is similar to 1976, and, therefore, we anticipate increases in major income categories of 15% to 25% and a capital expenditures increase of around 25%.





CANADIAN RESERVE OIL AND GAS LTD.
(Incorporated under the laws of the Province of Alberta)

BALANCE SHEET DECEMBER 31, 1976 and 1975

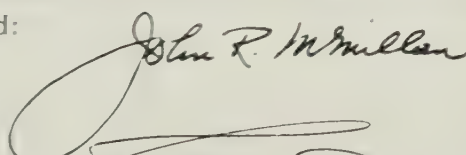

ASSETS

	1976	1975
CURRENT:		
Cash and term deposits	\$ 1,015,875	\$ 1,846,930
Accounts receivable	4,727,327	4,301,522
Inventory of sulphur and crude oil, at estimated net realizable value	1,151,576	1,197,781
Materials and supplies, at average cost	1,076,765	824,196
Prepaid expenses	61,699	32,802
	8,033,242	8,203,231
SUNDRY INVESTMENTS AND DEPOSITS (at the lower of cost and market)	117,157	97,733
PROPERTY AND EQUIPMENT:		
Oil and gas properties	47,178,701	39,733,950
Production equipment	12,143,187	10,845,888
Plants, pipelines and other equipment	7,496,549	7,896,936
	66,818,437	58,476,774
Less:		
Accumulated depletion	14,436,383	12,638,215
Accumulated depreciation	7,201,111	7,113,623
	45,180,943	38,724,936
	\$53,331,342	\$47,025,900

LIABILITIES AND SHAREHOLDERS' EQUITY

CURRENT:		
Accounts payable and accrued expenses	\$ 2,097,387	\$ 2,572,275
Due to affiliated companies	516,489	—
Current portion of bank production loans (Note 2)	600,000	600,000
Income taxes payable	900,000	1,750,000
	4,113,876	4,922,275
BANK PRODUCTION LOANS (Note 2)	890,000	490,000
DEFERRED INCOME TAXES	10,920,000	9,420,000
SHAREHOLDERS' EQUITY:		
Share capital (Note 3) —		
Authorized:		
20,000,000 common shares having a nominal or par value of \$1.00 each		
Issued:		
9,640,437 shares (1975 — 9,635,037)	9,640,437	9,635,037
Contributed surplus	5,899,552	5,888,725
Retained earnings	21,867,477	16,669,863
	37,407,466	32,193,625
	\$53,331,342	\$47,025,900

On behalf of the Board:

 Director.
 Director.

See accompanying notes.


Statement of Income

Years Ended December 31, 1976 and 1975

	1976	1975
Revenue:		
Gross operating revenue	\$15,855,752	\$13,393,756
Other	255,276	162,602
	16,111,028	13,556,358
Expenses:		
Operating	3,989,500	3,194,776
General and administrative	1,257,888	1,131,727
Depreciation	908,626	752,649
Depletion	1,798,168	1,413,052
Interest —		
Bank production loans	185,976	199,717
Other	153,418	—
Other	109,247	145,103
	8,402,823	6,837,024
Income before income taxes	7,708,205	6,719,334
Income taxes:		
Current	1,010,591	1,750,000
Deferred	1,500,000	650,000
	2,510,591	2,400,000
Net income for the year	\$ 5,197,614	\$ 4,319,334
Net income per share (Note 5)	\$0.54	\$0.45

Statement of Retained Earnings

Years Ended December 31, 1976 and 1975

	1976	1975
Balance, beginning of year	\$16,669,863	\$12,350,529
Net income for the year	5,197,614	4,319,334
Balance, end of year	\$21,867,477	\$16,669,863

Statement of Changes in Financial Position
Years Ended December 31, 1976 and 1975

	1976	1975
Source of funds:		
Net income for the year	\$5,197,614	\$4,319,334
Depletion, depreciation, deferred income taxes and other non-cash items, net	4,203,428	2,827,393
Cash flow from operations	9,401,042	7,146,727
Increase in long term portion of bank production loans	400,000	—
Proceeds from sale of property and equipment	18,120	27,760
Issue of share capital for cash	16,227	—
	9,835,389	7,174,487
Application of funds:		
Additions to property and equipment	9,177,555	5,275,725
Acquisition of investments	19,424	483
Repayment of bank production loans	—	1,600,000
	9,196,979	6,876,208
Increase in working capital	638,410	298,279
Working capital, beginning of year	3,280,956	2,982,677
Working capital, end of year	\$3,919,366	\$3,280,956

Statement of Contributed Surplus
Years Ended December 31, 1976 and 1975

	1976	1975
Balance, beginning of year	\$ 5,888,725	\$ 5,888,725
Consideration over par value for shares issued during the year	10,827	—
Balance, end of year	\$ 5,899,552	\$ 5,888,725



Notes to Financial Statements

December 31, 1976

1. Summary of significant accounting policies

Property and equipment —

The Company follows the full-cost method of accounting wherein all costs related to the exploration for and the development of oil and gas reserves, whether productive or non-productive, are capitalized. These costs are accumulated in two cost centres, Canada and the Middle East. Depletion is provided each year on costs accumulated in the Canadian centre by relating the total production for the year to the total estimated proven reserves (the composite unit of production method). Expenditures incurred in the Middle East are being deferred pending the results of exploration in progress in the area. These costs will be depleted on the basis of reserves discovered in the area or written off to income if exploration activities prove unsuccessful.

Depreciation of production equipment is provided on the same basis as depletion. Plants, pipelines and the majority of other equipment are depreciated on the straight line method at rates varying from 5% to 10%.

2. Bank production loans

Bank production loans are secured by certain producing properties and repayments in the

amount of approximately \$600,000 are required annually.

3. Share capital

Stock option plan —

During the year, options to purchase 27,000 shares were granted and options to purchase 12,600 shares were cancelled. 5,400 shares were issued for a cash consideration of \$16,227 as a result of options exercised during the year. At December 31, 1976 options granted to officers and employees to purchase 178,500 shares were outstanding. These options are exercisable at various dates to April 1985 at prices of \$2.03, \$3.20 and \$3.42 per share. In addition, the Company has reserved 61,200 shares for the granting of future options to officers and employees.

4. Statutory information

Directors and senior officers (including the five highest paid employees) received remuneration and benefits amounting to \$322,217 during 1976.

5. Net income per share

Net income per share is based on the average number of shares outstanding during the year. The exercise of the outstanding share options would have no dilutive effect.

AUDITORS' REPORT

To the Shareholders of
Canadian Reserve Oil and Gas Ltd.

We have examined the balance sheet of Canadian Reserve Oil and Gas Ltd. as at December 31, 1976 and the statements of income, retained earnings, contributed surplus and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion these financial statements present fairly the financial position of the company as at December 31, 1976 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Calgary, Canada.
February 3, 1977.

Curtis Young, Clouston, Gordon & Lee

Chartered Accountants.

FIVE YEAR SUMMARY

	1976	1975	1974	1973	1972
FINANCIAL					
Gross Revenue	\$16,111,028	\$13,556,358	\$10,760,945	\$8,999,791	\$7,360,246
Cash Flow	9,401,042	7,146,727	6,567,569	5,373,653	4,685,420
Depreciation and Depletion	2,706,794	2,165,701	2,498,557	2,618,174	2,153,317
Deferred Taxes	1,500,000	650,000	2,100,000	1,060,000*	952,000*
Net Income	5,197,614	4,319,334	1,946,343	1,629,780*	1,381,049*
Per Share					
Gross Revenue	1.67	1.41	1.12	.94	.77
Cash Flow98	.74	.68	.56	.49
Net Income54	.45	.20	.17*	.14*
Property and					
Equipment Additions	9,177,555	5,275,725	5,097,399	7,693,790	5,661,141
Working Capital	3,919,366	3,280,956	2,982,677	1,407,588	2,534,424
Outstanding Shares	9,640,437	9,635,037	9,635,037	9,613,397	9,526,282
OPERATING					
Oil and Gas Liquid Sales —					
Gross Working Interest	1,819,981	2,190,688	**	**	**
Barrels Per Day	4,973	6,002	**	**	**
Net Working Interest	1,413,884	1,772,468	2,069,679	2,383,771	2,333,792
Barrels Per Day	3,863	4,856	5,670	6,531	6,377
Gas Sales — Mcf					
Gross Working Interest	7,818,312	7,266,045	**	**	**
Mcf Per Day	21,362	19,907	**	**	**
Net Working Interest	5,841,233	5,589,294	6,070,998	5,937,703	6,691,018
Mcf Per day	15,960	15,313	16,633	16,268	18,282
Sulphur Sales — Long Tons					
Gross Working Interest	59,600	42,295	**	**	**
Long Tons Per Day	163	116	**	**	**
Net Working Interest	49,494	35,850	30,460	39,645	47,330
Long Tons Per Day	135	98	83	109	129
Wells Drilled — Gross (net)					
Oil	21(8)	23(12)	19(6)	62(19)	83(29)
Gas	48(10)	7(2)	14(4)	17(6)	10(2)
Dry	30(12)	26(10)	34(12)	43(18)	37(12)
Total	99(30)	56(24)	67(22)	122(43)	130(43)

*Restated for change in deferred tax accounting policy.

**Gross working interest figures not available prior to 1975.



**CANADIAN RESERVE
OIL AND GAS LTD.**
1976 ANNUAL REPORT